

said commodity and transferring a right to collect against said second insurance instrument to said second bidder if said second bidder exceeds said second price by a greater amount than said first bidder exceeds said first price.

REMARKS

This paper is responsive to the Office Action mailed October 10, 2001. Reconsideration of the subject application is respectfully requested based on the above Amendments and following Remarks.

Claims 9, 11, 13 and 14 have been amended to reflect corrections to informalities noted by the Examiner.

All pending claims 1-15 currently stand rejected, either under 35 USC § 102 or 35 USC § 103, based on Richter.

Applicant respectfully traverses the above rejections. First, a summary of the subject invention is provided. In a tier-priced industry, the use of an **insurance** instrument can guarantee commodity delivery and lower the cost of delivering the commodity. A buyer purchases a tier-priced commodity bundled with an **insurance** instrument from a commodity seller. In this example the buyer negotiates the purchase of the bundled commodity and **insurance** instrument with the commodity seller. The **insurance** instrument would be triggered and executed to absorb the additional costs of purchasing spot power under the conditions described in the **insurance** instrument. In the preferred embodiment the tier-priced commodity is electrical power being sold by a generating utility or broker. The buyer may be any consumer of the purchased commodity (i.e. an individual, a large manufacturing concern, a rural cooperative, a municipality, another generating utility or a reseller/broker) and the seller may be a commodity generating

utility or commodity reseller. In one embodiment, the **insurance** instrument is offered by the commodity provider along with the commodity as a bundled product (the purchase price of the commodity includes the purchase price of the **insurance** instrument used to guarantee the delivery of the commodity). In an alternative embodiment, the buyer purchases the **insurance** instrument and the commodity separately. In this example the **insurance** instrument is purchased from a broker such as an insurance company or financial institution.

More specifically, an **insurance** policy can be used to protect against an interruption in service to a customer (in this example a municipality). A municipality purchases interruptible power from a generating utility. The municipality has also purchased an **insurance** policy as part of a bundled product from the generating utility or an insurance company. If there is no interruption in service then the municipality receives its power as contracted from the generating utility and there is no need to purchase spot power from another utility (or power pool).

Purchasing a commodity supported by an **insurance** policy allows the municipality to purchase power at a reduced interruptible rate. The **insurance** policy takes effect if there is an interruption in service governed by the terms of the policy. Typically, the terms of the **insurance** policy will cover foreseeable interruptions and not force majeure events. The **insurance** policy is designed to take into account the risks associated with purchasing interruptible power. These risks include historical data regarding the weather and forecast conditions (such as heat waves) in and around the municipality (the consuming area), scheduled construction or maintenance shutdowns, the current/predicted future capacity of the generating utility and the current/ predicted future demands of the municipality (the load profile). If there is an interruption in service, the **insurance** policy will provide the finances necessary to allow the generating utility to purchase

or generate needed power to supplement the interruption. In the case where the municipality holds the **insurance** policy (purchased it separately from the commodity) the financial proceeds of the policy are paid to the generating utility or an alternative source or a transmitting utility to augment supply by purchasing or generating additional power. With the **insurance** policy covering the cost of purchasing expensive spot power, the alternative source (the providing utility or power pool) would transfer the supplemental power to the municipality through the generating utility or through another system (transmitting/distributing utility) depending upon the circumstances.

When a municipality (or any customer for that matter) is the **insurance** policy holder, an agreement among the electricity provider, the insurance provider, and the end-user would be structured to provide interruptible power under a mutually acceptable set of circumstances. This agreement allows the generating utility, through their trading floor, to purchase power for interruptions on behalf of the municipality (including the end users), using funds provided by the insurance policy held by the municipality. In an alternative embodiment the end-users would contract directly with the generating utility and the insurance provider.

Thus, independent claims 1, 9, 12, 13, 14 and 15 either explicitly or implicitly all require:

- a. determining a first price for a commodity at a first tier;
- b. determining a second price for said commodity at a second tier;
- c. **determining a third price for an insurance instrument designed to indemnify against at least one risk associated with purchasing said commodity at said second tier; and**

d. offering said commodity at said second tier for sale at a fourth price; wherein
said fourth price is a function of at least said second price and said third
price.

Richter neither discloses nor suggests “determining a third price for an insurance instrument designed to indemnify against at least one risk associated with purchasing said commodity at said second tier” nor “offering said commodity at said second tier for sale at a fourth price, wherein said fourth price is a function of at least said second price and said third price.” Richter relates to **options** and **futures** for **spot** energy prices. Richter makes no mention of **insurance** instruments to bridge the price groups between **non-spot** energy **price tiers**. A summary of Richter follows.

According to Richter, traders will find it helpful to create and implement bidding strategies to make their bids and offers. Bidding strategies may be designed to limit the trader’s risk, to maximize profit, or some combination of both. Richter’s paper focuses on developing bidding strategies to maximize profit for the **spot market** using genetic algorithms and genetic programming. Richter’s previous research focused on double auction bidding strategies for the **spot market**, the techniques may be used in the **futures**, **options** and **forwards** markets. In this paper, Richter extends previous work by creating energy trader portfolios which combine the **spot market contracts** with **options** and **futures contracts** to manage the trader’s risk and profitability.

The **spot market** allows for trading power **each hour** (or other duration, e.g., 30 minutes) in the next 30 days. Forward contracts allow energy traders to buy or sell firm electricity contracts as specified in the contract from 1 to 19 months into the future. The futures market

allows traders to purchase a non-firm electricity contract for a given month, 1 to 18 months into the future. Futures contracts provide a means for electricity traders to manage their risk. The planning market is a longer term market used to develop capital for building new plants and transmission lines.

As the electric energy marketplace deregulates, many experts expect the cash market to be joined by markets specializing in **futures contracts, options contracts, and planning contracts**. A swaps market will enable these contracts to be traded to maximize trader utility. According to Richter, the **spot market** is what we are most familiar with in the electrical industry. A seller and a buyer agree (either bilaterally or through an exchange) upon a price for a certain number of MWs to be delivered sometime in the near future (e.g., 10 MWs from 1:00 p.m. to 4:00 p.m. tomorrow). The buyer needs the electricity, and the seller wants to sell. They arrange for the electrons to flow through the electrical transmission system and they are happy. A **forwards contract** is a binding agreement in which the seller agrees to deliver an amount of a particular product with a specified quality at a specified time to the buyer. The forwards contract is further into the future than is the spot market. In both the forwards and spot contracts, the buyer and seller want to exchange the physical good (e.g., the electrons). A **futures contract** is primarily a financial instrument which allows traders to lock-in a price for a commodity in some future month. This helps the traders to manage their risk by limiting potential losses or gains. Futures contracts exist for commodities in which there is sufficient interest, and in which the goods are generic enough that it is not possible to tell one unit of the good from another (e.g., 1 MW of electricity of a certain quality, voltage level, etc.) A futures **options contract** is a form of insurance that gives the option purchaser the right, but not the obligation, to buy (sell) a futures

contract at a given price. For each options contract, there is someone “writing” the contract who in return for a premium, is obligated to sell (buy) at the strike price. See Fig. 3. Both the options and the futures contract are financial instruments designed to minimize risk. Although provisions for delivery exist, they are not convenient (e.g., the delivery point is not located where you want it to be located). The trader ultimately cancels his position in the futures market either with a gain or loss. The physicals are then purchased on the spot market to meet demand with the profit or loss having been locked in via the futures contract. A *swap* is a customized agreement in which one firm agrees to trade its coupon payment for that of the other firm involved in the swap. Finally, we have the *planning market* which exists to finance long term projects like transmission lines and power plants.

According to Richter, **futures contracts** allow producers to hedge so that they can limit their losses. Other things being equal, a GENCO’s (producer) profit varies with the price of electricity. Trying to predict the price months in advance so that profit can be known in advance is tricky. Suppose it is April, and because of some big decisions (unrelated to insider trading) the board-members want to know what the GENCO’s profit will be in July. Simply by considering our fuel contracts and using demand forecasts we can draw a profit curve based on the price. Not knowing the price means that we have the potential for large losses. The board-members don’t want to see just a line on a graph—they want a simple number. This is where the futures hedging comes into play. The GENCO can short (i.e. sell non-firm electricity they don’t have yet) July electricity with futures contracts. When July arrives, if the **spot price** is low, they make money on their futures contract and lose on the electricity sold on the **spot market**. The gain on the futures market offsets the loss in the **spot market**. If the **spot price** in July is high, then the

electricity sold on the spot market yields a profit while the futures contract will product an offsetting loss. The result is that the net profits profit is much more predictable due to the hedge, and now we can give the board-members that number they were looking for.

i. Richter Does Not Provide For “An Insurance Instrument To Indemnify Against A Risk.”

The above language is a limitation in all of Claims 1-15. Claims 1-15 stand rejected based upon Richter solely because of the use of “financial instrument” in Richter. However, a cursory reading of Richter reveals that the “financial instruments” discussed therein are option contracts, i.e. put and call options, that are only useful in the spot commodities market. In contrast, the subject invention, as now defined by the claims, focuses on **insurance** instruments to provide a price bridge between two price tiers of energy if an event occurs that necessitates the purchase of energy at a higher price tier. The differences between insurance instruments and option contracts are numerous in nature and are the fundamental underpinnings for the presence of two entirely separate and autonomous multi-billion dollar financial institutions. If this were not the case, the two separate financial institutions would not even exist, but instead we would have option contracts **or** insurance policies. Suffice it to say that an insurance policy sets out the rights and duties of the insurer and the insured and provides monetary compensation for losses or damages upon the occurrence of a defined event, while option contracts merely allow the sale or purchase of a commodity at an arbitrary price within a predetermined time period **regardless** of the occurrence of any events. Insurance can be payed in a lump sum or at different times during the continuance of the risk. The number and types of risks that can be insured encompass practically every conceivable form or kind. The nature of the risk is assumed by the party in the

party in the role of the insurer and is controlled by chance or nature. The determination of an insurance policy involves statistical risk assessment and may provide for a series of risks or broad comprehensive coverage. Benefits provided in an insurance policy can be specifically stated, along with a maximum or minimum amount that will be payable, and temporary coverage can be provided by a binder that states that a policy of insurance is in force. The insurer is the primary party liable upon occurrence of the contingency and must bear the ultimate loss. None of the above qualities necessary to constitute an insurance instrument is present in an option contract.

Thus, Richter does not relate to **insurance instruments that indemnify against risk upon the occurrence of a defined event in any way.**

ii. Richter Does Not “Offer The Commodity At The Second Tier Where A Fourth Price Is A Function Of At Least The Second Price And The Third Price.”

The above language, required by all of claims 1-15 either identically or equivalently, is neither disclosed nor suggested by Richter. Richter does not relate to static, relatively fixed **multiple** price “**tiers**”. Instead, Richter is concerned with dynamic “**spot markets**” where the price for a commodity **within a single** tier (i.e. the interruptable power tier, as opposed to the firm power tier) fluctuates. However, the present invention, in contrast, is focused on bridging the price gap **between two different** price **tiers** upon the occurrence of a defined event through the use of an insurance instrument. Non-limiting examples of some of the different, separate “**tier**” levels contemplated by the present invention (“firm,” “interruptible” and “spot”), all

known in the industry as separate price levels defined by associated risk, are provided on pages 2-4 of the specification as originally filed.

Hence, claims 1-15 of the present invention, offer the commodity at a **price not contemplated by Richter** because the subject claims perform the following not disclosed or suggested by Richter:

- (1) determining a first price for a commodity at a **first tier**;
- (2) determining a second price for a commodity at a **second tier**;
- (3) determining a third price for an **insurance instrument**; and
- (4) **offering the commodity for sale at a fourth price** that is a function of the **first tier price** and the **insurance instrument price**.

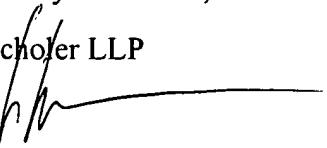
Claims 1-15 are thus neither anticipated nor obvious in light of Richter because one could not derive the **fourth price** of the commodity based on the **first tier price**, **second tier price** and **insurance instrument price** by employing Richter. Specifically, there is no relation in Richter between the profit (or loss) of the option contract and the monetary value of the first tier price, as there is in the present invention in which the commodity price (fourth price) is based on these two money factors (the first tier price and the insurance instrument price).

For the reasons stated above, applicant respectfully requests allowance of the subject application.

Respectfully submitted,

Kaye Scholer LLP

By


John M. Johnson
Reg. No. 33,334